IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1978
No. 78-1577

Supreme Court, U.S.
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MICHAEL RODAK, JR., CLERK

SEARS, ROEBUCK & CO., a corporation

Petitioner,

vs.

COUNTY OF LOS ANGELES and
CITY OF COMPTON,

Respondents.

Brief of Amicus Curiae Pioneer Electronics of America, Soundesign Western, Association of Electronic Importers, and Foreign Trade Association of Southern California, in Support of Petitioner Sears, Roebuck & Co.

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INTEREST OF AMICUS

Pioneer Electronics of America, Soundesign Western, the Association of Electronic Importers, and the Foreign Trade Association of Southern California hereby respectfully file this Brief Amicus Curiae in support of Petitioner Sears, Roebuck & Co. and consent of both parties was obtained by the attorneys for Amicus Curiae and

are attachted hereto as Appendices A and B.

Pioneer Electronics of America and Soundesign Western are domestic corporations importing goods into the State of California, a substantial portion of which is transshipped out of the State, and transshipment exemptions under California Revenue and Taxation Code Section 225 have been claimed, and are pending before the courts of the State of California. These claims are dependent upon the outcome of this case.

Amicus Curiae Association of Electronic Importers is a California corporation consisting of electronic importers, all of whom have inventories in the State of California, transshipped a portion of such inventories out of the State, and fall within the provisions of Revenue and Taxation Code Section 225.

Amicus Curiae Foreign Trade Association of Southern California is a nonprofit association of more than 460 importers, exporters and service firms engaged in international trade and vitally interested in the impact and effect this litigation has had and will have on the importing industry and international trade.

Attorneys for Amicus Curiae represent the above corporations and numerous companies that have claimed transshipment exemptions under the provisions of California Revenue and Taxation Code Section 225 and have lawsuits pending against the County of Los Angeles for recovery of exemptions which have been denied. Said attorneys are

familiar with all of the issues, briefs and facts in this case, and represented Zee Toys, the companion case to Sears, Roebuck & Co. v. County of Los Angeles.

QUESTION PRESENTED

Whether California Revenue and Taxation Code Section 225, in granting a property tax exemption to imported inventories no longer in transit, but inteded for transshipment out of the State of California, regulates interstate and foreign commerce and thereby violates the Commerce Clause of the United States Constitution.

SUMMARY OF ARGUMENT

1. The purpose of the Commerce Clause is to prevent states from discriminating against interstate or foreign commerce in favor of local business or commercial interests. Exempting certain classes of inventory does not provide any commercial advantage to a local business in violation of the Commerce Clause purposes.

2. For a state tax statute or regulation to be found unconstitutional under the Commerce Clause there must be an affirmative showing that it has burdened commerce in a manner violating the intent and purposes of the Commerce Clause. The court in the instant case has merely assumed or speculated that there was a burden because a

distinction, classification, or discrimination existed.

3. The use of a per se test to determine constitutionality of a statute under the Commerce Clause has been rejected by this Court. Reliance by the court in Zee Toys on Boston Stock Exchange v. State Comm'r., 429 U.S. 318 (1977) is misplaced.

4. There is no constitutional impediment to classifying types of goods for different tax treatment. A state may constitutionally tax some goods and exempt others based on the type of goods involved, their manner of manufacture or even their place of origin. Such distinctions are constitutional so long as the state has not attempted to discriminate against interstate or foreign businesses.

ARGUMENT

A. THE CALIFORNIA COURT OF APPEAL HAS NOT PROPERLY APPLIED THE COMMERCE CLAUSE.

The California Court of Appeal held that California's free port or transshipment law, Revenue and Taxation Code Section 225, violated the Commerce Clause of the U.S. Constitution. The basis of the court's holding was that an exemption was provided for goods imported

from foreign countries, but not similarly provided to goods imported from other states. This, reasoned the court, constituted a discrimination and a burden on interstate commerce, an inpermissible regulation of foreign commerce, and an interference with the federal government's pattern of imposing import duties.

In reaching this decision the court has misconstrued the purposes of the Commerce Clause. It should be noted that the goods in the instant case were no longer in foreign commerce or in interstate commerce. They were unloaded from vehicles of transportation and placed in warehouses for storage pending subsequent transshipment to retail stores, and were subject to the state's power to impose a nondiscriminatory ad valorem property tax. Michelin Tire Corp. v. Wages, 423 U.S. 276 (1976). Unlike Michelin, the question is not whether the state can tax such goods, but whether it must tax such goods, together with other inventory in the state. It should also be noted that Section 225 does not distinguish between local business and interstate or foreign businesses: each is entitled to the exemption to the extent it deals in foreign goods. Section 225 is merely a classification statute; granting an exemption to certain types of goods and denying it to other types of goods.

The purpose of the Commerce Clause is to see that states do not discriminate against interstate or foreign commerce by giving local businesses commercial advantage over out-of-state businesses. (See, e.g., H. P. Hood & Sons, Inc. v. Du Mond, 336 U.S. 525, 538-539

(1949).) In Japan Lines, Ltd. v. County of Los Angeles, ___ U.S. ___, 60 L.Ed.2d 336 (1979), the Court noted that in regard to foreign commerce the Import-Export Clause and Commerce Clause had similar policies: (1) to permit the federal government to speak with one voice in commercial relations with foreign governments; (2) to prevent the states from diverting revenues from the federal treasury to their own treasuries; and (3) to prevent port states from exacting unreasonable tolls to the rest of the country. None of those policies are violated by an exemption statute as opposed to a tax.

As distinguished from Japan Lines, in the instant case there was no evidence of any adverse or potential effect on interstate or foreign commerce. To the contrary, Section 225 by providing an exemption would not provide any risk of retaliation from foreign countries, but invites reciprocity of tax treatment for United States exports.

In McGoldrick v. Berwind-White Coal Mining Co., 309 U.S. 33, 48 (1940) the Court held that the law under the Commerce Clause had been fashioned by the Court in an effort to "'. . . reconcile competing constitutional demands, that commerce between the states shall not be unduly impeded by state action, and that the power to lay taxes for the support of state government shall not be unduly curtailed.'" The balance between the competing demands of state interests and the constitutional requirements of the Commerce Clause have been accomplished by upholding taxes designed to make interstate commerce bear a reasonable share of the cost of local government,

and "by invalidating those which discriminate against interstate commerce, which impose a levy for the privilege of doing it, which impose an undue burden on it." (American Smelting, Etc. Co. v. County of Contra Costa, 271 Cal. App. 2d 437, 77 Cal. Rptr. 570 (1969).)

The instant case does not discriminate, but merely supplies an exemption. The principal purpose of the Commerce Clause, to prevent states from obstructing foreign and interstate commerce, has not been abused. While a tax can burden foreign commerce and obstruct commercial intercourse, a tax exemption has no such effect. The error of the court in the instant case was its failure to make a fundamental analysis of a state regulation which places no undue burden on commercial is established. The test in any event must be whether or not the distinction created by the statute creates an undue risk of burden to interstate or foreign commerce. When relations with foreign governments are involved, an added test is whether the tax or regulation under consideration will prevent the federal government from speaking with a single voice. (Japan Lines, Inc. v. County of Los Angeles, supra.) Neither of these criteria are threatened in the instant case.

Before a state statute or regulation can be declared unconstitutional under the Commerce Clause, it must be shown to have burdened the commerce involved, whether it is interstate or foreign commerce. (See, Halliburton Oil Well Cementing Co. v. Reily, 373 U.S. 64, 69 (1963).) In McGoldrick v. Berwind-White Coal Mining Co.,

supra, at 45, the Court stated: "It is only when the tax operates to regulate commerce between the states or with foreign nations to an extent which infringes the authority conferred upon Congress, that the tax can be said to exceed constitutional limitation. [citations]"

By contrast to Halliburton, Japan Lines and McGoldrick, the Zee Toys court made no showing of a burden on commerce. Instead, the court held that there was a "discrimination" and applied a per se test.

The use of a per se test in the instant case is in contrast to the modern trend of decisions allowing greater latitude to states in instituting their taxing policies. (See, Michelin Tire Corp. v. Wages, supra; Complete Auto Transit, Inc. v. Brady, 430 U.S. 274 (1977).)

In Washington Revenue Dept. v. Association of Washington Stevedoring Companies, 435 U.S. 734 (1978), this Court overruled Puget Sound Stevedoring Co. v. Tax Commissioner, 302 U.S. 90 (1937), and put to rest the direct-indirect test, reiterating the necessity to balance the burden placed on interstate commerce by the benefit to the state. This Court stated:

> "Respondents, therefore, have demonstrated no impediment imposed by the tax upon the regulation of foreign trade by the United States."
> 435 U.S. at 754.

In Moorman Manufacturing Co. v. Blair 437 U.S. 267 (1978), this Court pointed out that

states have wide latitude in the selection of appropriate formulas, which will be disturbed only in the event of clear evidence that the methods being used were unreasonable.[1/]

[1/] Moorman Manufacturing upheld a single factor formula applied by the state in attributing income taxes. The case emphasizes the broad ramifications which the instant case may have upon a wide spectrum of tax statutes.

California is one of the few states that requires U.S.-based and foreign-based multinational corporations to file a unitary or combined income tax return. Such requirements have had an increasingly adverse effect on the California business climate, and there is pending in the California Legislature Assembly Bill 525, which would eliminate such unitary or combined reporting for foreign-based multinationals. Domestic multinational corporations would not be affected. The rationale for such distinction is the more onerous burdens placed on foreign-based umltinationals by having to translate into U.S. accounting standards all their activites and in translating their world-wide incomes to U.S. currency.

In discussing the Zee Toys decision in testimony before the Assembly Revenue and Taxation Committee November 13, 1979, Ben Miller, counsel for the California Franchise Tax Board, stated:

(continued on p. 10)

In the instant case the court placed great reliance on Boston Stock Exchange v. State Tax Comm'r., 429 U.S. 318 (1977). The court, however, has misconstrued the Boston Stock Exchange case in stating that: "In that case, a state tax which discriminated against two types of interstate transactions was struck down." (Pet. Appendix p. 15.) The court overlooked that the vice in the Boston Stock Exchange case was the attempt by the State of New York to design a tax program which would provide a commercial advantage to local businesses (New York stock

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1/ (continued from previous page)

> "The California Appellate Court invalidated a state statute which exempted certain products shipped in foreign commerce from property taxation. The court held that the statute unconstitutionally discriminated in favor of foreign commerce, vis-a-vis interstate commerce. The court's reasoning might invalidate any efforts by the Legislature to place limitations on the application of the unitary concept based upon the geographic location of the operations.
>
> . . .
>
> "Based upon the court's holding [in Zee Toys], any attempt to limit the application of the unitary method, with respect to foreign-based businesses, would probably be constitutionally invalid." (Emphasis added.)

exchanges) to the detriment of out-of-state stock exchanges. This Court cautioned:

> "On various occasions when called upon to make the delicate adjustment between the national interest and free and open trade and the legitimate interest of the individual States in exercising their taxing powers, the Court has counseled that the result turns on the unique characteristics of the statute at issue and the particular circumstances in each case." (429 U.S. at 329.)

Under California's Free Port Law there is no distinction betwen out-of-state and in-state residents or businesses. Both are given the economic advantages of the Free Port Law, and any use by the court of a per se test was improper and misconstrued the Commerce Clause of the United States Constitution.

B. DISTINGUISHING BETWEEN GOODS BASED ON THEIR ORIGIN DOES NOT VIOLATE THE COMMERCE CLAUSE OF THE UNITED STATES CONSTITUTION.

The Court of Appeal based its holding on the following observation:

"Different tax treatment is, therefore, accorded to such goods solely on the basis of their place of origin. Foreign goods are thereby given a competitive advantage over interstate goods of the same nature and competing in the same market." (Pet. Appendix p. 11.)

There was no evidence of any competitive advantage. However, assuming for argument that there would be such a competitive advantage, it is submitted that this in and of itself does not violate the Commerce Clause, and that such distinctions are commonplace.

In Raley & Bros. v. Richardson, 264 U.S. 157 (1924), this Court upheld a Georgia tax upon brokers or commission merchanges dealing in intrastate goods, which tax was not imposed upon similar brokers dealing in goods originating in interstate commerce. This Court rejected arguments that such distinction violated the Commerce Clause. It is submitted that there is no distinction between the discrimination permitted in Raley & Bros. and the discrimination in the instant case. Neither places unreasonable burdens on interstate or foreign commerce, and neither violates the purposes of the Commerce Clause.

C. ZEE TOYS IS IN CONFLICT WITH OTHER STATE COURT DECISIONS WITH RESPECT TO THE CONSTITUTIONALITY OF FREE PORT LAWS.

All states encourage local industry by providing tax exemptions. Examples are domestic wines while aging in California, dairy products in Wisconsin, certain fish products in Louisiana, and wheat products in the Midwestern states. With increasing frequencies states have been providing exemptions to inventories, and especially inventories stored for transshipment. "Not only are inventories exempt in the few but very important states that exempt all personal property . . . but they are wholly or partially exempt if they have been brought into a state for storage or other limited activities before being shipped out of the state." (National Tax Journal, Property Tax Developments: Modernization, Classification, Site Value Taxation, 19:322, 324 (Sept. 1976).)

Such classification statutes are generally tested under Equal Protection principles. In the instant case the Court of Appeal conceded that if Los Angeles County were only invoking an Equal Protection argument, it could not prevail, since a rational basis existed for the distinction.

Over 35 states have some type of free port exemption. A substantial number of these statutes grant out-of-state or foreign products an exemption

which is denied to similar products manufactured or grown in the United States or in the state in question. These distinctions are based on the origin of the goods, the same distinction struck down in the instant case.

Amicus knows of no other instance in which a free port statute has been held unconstitutional.

In Appeal of Martin (S. Ct. N. C., 1974) 209 S. E. 2d 766, the court upheld a statute providing the following exemptions:

1. Cotton, tobacco, other farm products, goods, wares and merchandise held for shipment to any foreign country or stored at a seaport awaiting further shipment after being imported from a foreign country.

2. Personal property of nonresidents in their original package shipped into the state and placed in a public warehouse for the purpose of transshipment to a destination either outside of the state or within the state.

3. Personal property of residents in their original package placed in a public warehouse for transshipment, but only to an out-of-state destination. (G. S. §105-281 (1969)(Cum. Supp.)

The North Carolina statute discriminated based on the origin of the goods and based on the residence of the owner of the goods. The statute specifically described its purposes:

> "It is hereby declared to be the policy of this state to use its system of property taxation in such manner, through the classification of the aforementioned property, as to encourage the development of the ports of North Carolina . . . [and] to encourage the development of the State of North Carolina as a distribution center." (Emphasis added.)

Under the North Carolina statute a distributor, such as petitioner or either individual amicus, who warehouse in non-public facilities would: (a) be taxed on goods purchased domestically; (b) be given an exemption on imported goods. This is the same distinction struck down in the instant case.

In State Bd. of Tax Comm'rs. v. Carrier Corp. (S. Ct. Ind. 1977) 365 N. E. 2d 1385, ad valorem property tax exemptions were upheld under a statute almost identical to the one reviewed in The Appeal of Martin. In a petition for rehearing the court held that the statute did not unreasonably burden interstate commerce. (State Bd. of Tax Comm'rs. v. Carrier Corp. (S. Ct. Ind., 1977) 365 N. E. 2d 1153.)

If, in the instant case, the Court of Appeal has accurately interpreted Boston Stock Exchange and Michelin Tire Corp., then both the North Carolina and Indiana taxing schemes would also have to fail for violating the Commerce Clause.

In Nash Sales v. City of Milwaukee (S. Ct. Wisc., 1929) 224 N. W. 126, the State Legislature,

concerned about the competitive position of its warehousing industry, granted an exemption to property manufactured or produced outside of the state, and in storage in Wisconsin. The court held that there was no violation of the Commerce Clause, stating:

> "'The discretion of the Legislature in this field is so broad that it is not competent for the court to mark the constitutional limitations of it other than at the farthest one might go without transcending all reason.' [citation]" (at 129.)

In Allied Stores of Ohio v. Bowers, 358 U.S. 522, 3 L.Ed.2d 480, 79 S.Ct. 437 (1959), an Ohio statute exempted merchandise belonging to nonresidents held in storage but taxed similar property belonging to residents. This Court upheld the statute against Equal Protection arguments.

It is submitted that state classification statutes passed for the purpose of encouraging economic activity within the state do not violate the Commerce Clause merely by creating a distinction between types or classes of property. Only if the classification statute has as its purpose or effect favoring local business to the detriment of interstate or foreign businesses must a statute be tested under Commerce Clause statutes.

CONCLUSION

For the foregoing reasons the opinion of the Court of Appeal, Second Appellate District, should be reversed.

Respectfully submitted,

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APPENDIX A

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October 10, 1979

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Re: Sears, Roebuck & Co. v. County of Los Angeles
No. 78-1577

Dear Mr. Manpearl:

This will confirm that we have no objection and consent to your filing an Amicus Curiae Brief on behalf of Sears, Roebuck & Co.

Yours truly,

JOHN E. LARSON
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APPENDIX B

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October 10, 1979

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/s/ Frank M. Keesling
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